Private Causes of Action under the Recodified Texas Securities Act©

John R. Fahy
Whitaker Chalk Swindle Schwartz PLLC
Fort Worth, Texas
(817) 878-0547 or jfahy@whitakerchalk.com

State Bar of Texas
13th Annual
Essentials of Business Law
March 3, 2022

TABLE OF CONTENTS

John R. Fahy
Whitaker Chalk Swindle Schwartz PLLC
301 Commerce St., Suite 3500
Fort Worth, Texas
(817) 878-0547
jfahy@whitakerchalk.com

John R. Fahy is a member of Whitaker Chalk Swindle Schwartz PLLC in Fort Worth where he has worked since 2006. He chairs the Securities Committee of the State Bar of Texas's Business Law Section and has served as a Council Member for the Business Law Section. He worked for the U.S. Securities and Exchange Commission's Fort Worth District Office, managed the Texas State Securities Board's Houston office, and served as general counsel for two registered broker-dealers. He also previously held the Series 7, 24, and 66 licenses. He earned his law and masters degrees from the University of Texas and his B.A. from Yale.

Private Causes of Action under the Recodified Texas Securities Act©

The Texas Legislature passed the Texas Securities Act recodification in the 2019 regular session with an effective date of January 1, 2022.[1] The Legislature amended the recodified Texas Securities Act's private cause of action provisions through SB 1280 during the 2021 regular session by deleting cross-references imposing liability for violations as to six Texas Securities Act provisions that imposed no duties on private actors and thus had no potential for violations by private actors.[2] Business attorneys should have some familiarity with the recodified Texas Securities Act's private causes of action and remedies in order to properly advise clients of potential pitfalls in securities transactions. Business attorneys should also relearn the Texas Securities Act statutory structure, which has significantly changed. The previous Texas Securities Act had had 64 sections. The recodified Texas Securities Act ("Recodified TSA") has 248 sections - almost 400% more.

Basics of Securities Regulation and Liability

All securities transactions are required to be registered with the Texas Securities Commissioner by the sellers, unless exempt under the recodified TSA.[3] The sale of the security in a registered transaction does not cover the resale of the same security, as subsequent securities transactions must also either be registered or exempt.[4] The Recodified TSA has a private cause of action against the sellers of unregistered, non-exempted securities.[5]

Securities broker-dealers, broker-dealer agents, investment advisers or investment adviser representatives are required to be registered with the Texas State Securities Board unless exempt under the Recodified TSA and rules promulgated thereunder.[6] The Recodified TSA has a private cause of action against unregistered securities brokers who are acting as agents of sellers (unless

[1] HB 4171 (86th Texas Legislature, Regular Session, 2019).
[2] SB 1280 (87th Texas Legislature, Regular Session, 2021).
[3] Tex. Gov't Code §4003.001(a).
[4] *SEC v. Cavanagh*, 155 F.3d 129, 133 (2d Cir. 1998).
[5] Tex. Gov't Code §4008.051(a).
[6] Tex. Gov't Code §§4004.051(a), 4004.0052, 4004.101, and 4004.102.

exempt),[7] but not as agents of purchasers. It also has a private cause of action against unregistered investment advisers and investment adviser representatives (unless exempt).[8]

The Recodified TSA contains anti-fraud provisions with private causes of action with separate anti-fraud private causes of action provisions against sellers[9] and buyers.[10]

The Recodified TSA contains private causes of action for secondary liability against control persons and aiders, provided that the underlying primary violation has been proved, that applicable defenses have been waived or defeated for control persons[11] and materially aiding and a culpable mental state has been proven for aiders, and applicable defenses have been waived or defeated for aiders.[12]

Plaintiff Attorneys Will Find Advantages in using the Recodified TSA over the Securities Act of 1933 and the Securities Exchange Act of 1934

Texas business attorneys should know the Recodified TSA's private causes of action. Indeed, the Recodified TSA may be more advantageous to plaintiffs than the Securities Act of 1933 or the Securities Exchange Act of 1934. Here are some differences:

Issue	Recodified TSA	Securities Act of 1933 Securities Exchange Act of 1934
Securities Registration and Securities Broker-Dealer Registration Statute of Limitations	Three-year statute of limitations (no discovery rule) or one year after a rejected rescission offer with a preservation of the right to sue for both Securities Registration and Broker-Dealer Registration claims.[13]	Securities Registration – One-year statute of limitations[14] Broker-Dealer Registration – Most cases hold that there is no private cause of action (majority rule)[15]

[7] Tex. Gov't Code §4008.051(a).
[8] Tex. Gov't Code §§4008.059 and 4008.060.
[9] Tex. Gov't Code §4008.052.
[10] Tex. Gov't Code §4008.053.
[11] Tex. Gov't Code §4008.055(a) and (b).
[12] Tex. Gov't Code §4008.055(c); *Sterling Trust Co. v. Adderley*, 168 S.W.3d 835 (Tex. 2005).
[13] Tex. Gov't Code §4008.062(a).
[14] 15 U.S.C. §77m.
[15] 15 U.S.C. §78*o*(a); Cases holding no Securities Exchange Act of 1934 private cause of action for acting as an unregistered broker or dealer - *Asch v. Philips, Appel & Walden, Inc*., 867 F.2d 776, 777 (2nd Cir. 1989); *SEC v. Seaboard Corp., Admiralty Fund v. Hugh Johnson & Co.*, 677 F. 2d 1301, 1313–14 (9th Cir. 1982); *Brannan v. Eisenstein*, 804 F. 2d 1041, 1041 n.1 (8th Cir. 1986); *Bull v. Am. Bank & Trust Co. of Pa.*, 641 F.Supp. 62, 65 (E.D. Pa. 1986); *Sheldon v. Vermonty*, 204 F.R.D. 679, 684–85 (D. Kan. 2001); *Bamert v. Pulte Home Corp*., 202 U.S. DIST. LEXIS 112688, at *18 (M.D. Fla. 2012); *Olsen v. Paine, Webber, Jackson & Curtis, Inc.*, 623 F.Supp. 17, 18 (M.D. Fla. 1985); *Kidder Peabody & Co. Inc. v. Unigestion Int'l, Ltd*., 903 F. Supp. 479, 493–95 (S.D.N.Y. 1995). Cases holding a private cause of action under §15(a) - *Eastside Church of Christ v. National Plan, Inc*., 391 F.2d 357, 361-62 (5th Cir. 1968); *Landegger v. Cohen*, F. Supp. 3d 1278 (D. Colo. 2013). Note that the Fifth Circuit precedent (*Eastside Church of Christ*) dates from 1968 before the Supreme Court decided *Cort v. Ash*, 422 U.S. 66, 95 S. Ct. 2080, 45 L. Ed. 2d 26 (1975) in which it provided a new analytical framework for determining whether a statute has an implied private cause of action. That analytical framework is:

Issue	Recodified TSA	Securities Act of 1933 Securities Exchange Act of 1934
Securities Fraud Statute of Limitations and *Scienter*	Three-years after discovery; Five-year statute of limitations.[16] No *scienter* (culpable mental state) required.	Securities Fraud –Securities Act of 1933 – three-year statute of limitations.[17] Securities Fraud –Securities Exchange Act of 1934 - two years after the discovery and five years statute of limitations (*scienter* required)
Pleading Securities Fraud	No special pleading requirements to plead securities fraud	FRCP Rule 9(d) requires complainants to plead fraud with particularity, specifically the complaint must allege: "the time, place and contents of the false representation, as well as the identity of the person making the misrepresentation and what that person obtained thereby."[18] Rule 9(d) is intended to "provide defendants with fair notice of the plaintiffs' claims, protect defendants from harm to their reputation and goodwill, reduce the number of strike suits, and prevent plaintiffs from filing baseless claims and then attempting to discover unknown wrongs."[19]
Aiding Liability	Aiders can be liable for someone else's primary violation of the TSA provided a culpable mental state and substantial assistance is proved.[20]	No general private cause of action for aiding other's violations under Securities Act of 1933[21] and Securities Exchange Act of 1934.[22]

> In determining whether a private remedy is implicit in a statute not expressly providing one, several factors are relevant. First, is the plaintiff "one of the class for whose *especial* benefit the statute was enacted, -- that is, does the statute create a federal right in favor of the plaintiff? Second, is there any indication of legislative intent, explicit or implicit, either to create such a remedy or to deny one? Third, is it consistent with the underlying purposes of the legislative scheme to imply such a remedy for the plaintiff? And finally, is the cause of action one traditionally relegated to state law, in an area basically the concern of the States, so that it would be inappropriate to infer a cause of action based solely on federal law? (citations omitted) *Cort* at 78.

[16] Tex. Gov't Code §4008.062(b).

[17] 15 U.S.C. §77m.

[18] *IAS Servs. Grp., L.L.C. v. Jim Buckley & Assocs., Inc*., 900 F.3d 640, 647 (5th Cir. 2018) (quoting *United States ex rel. Grubbs v. Kanneganti*, 565 F.3d 180, 186 (5th Cir. 2009)).

[19] *Id.* (quoting T*uchman v. DSC Commc'ns Corp*., 14 F.3d 1061, 1067 (5th Cir. 1994)).

[20] Tex. Gov't Code §4008.055(c); *Sterling Trust* Co. *v. Adderley*, 163 S.W.3d 835 (Tex. 2005). "We therefore hold that the TSA's "reckless disregard for the truth or the law" standard means that an alleged aider can only be held liable if it rendered assistance "in the face of a perceived risk" that its assistance would facilitate untruthful or illegal activity by the primary violator. . . . In order to perceive such a risk, the alleged aider must possess a general awareness that his role was part of an overall activity that is improper."

[21] 15 U.S.C. §77*o*(b). See also Securities Act of 1933, Section 11(a)(4) providing for a private cause of action limited to registered offerings' professional's certifications and valuations in the registration statement or any report or valuation used in the registration statement. Claim is subject to affirmative due diligence defenses. 15 U.S.C. §77k(a)(4).

[22] *Cent. Bank of Denver v. First Interstate Bank of Denver*, 511 U.S. 164 (1994); *Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc.*, 552 U.S. 148, 156–58 (2008).

The Scope of the Texas Securities Act – Definition of Security

The Texas Securities Act applies to securities offers and transactions. The Recodified TSA defines "security" as follows:

Sec. 4001.068. SECURITY. (a) The term "security":
(1) includes:
(A) a limited partner interest in a limited partnership;
(B) a share;
(C) a stock;
(D) a treasury stock;
(E) a stock certificate under a voting trust agreement;
(F) a collateral trust certificate;
(G) an equipment trust certificate;
(H) a preorganization certificate or receipt;
(I) a subscription or reorganization certificate;
(J) a note, bond, debenture, mortgage certificate, or other evidence of indebtedness;
(K) any form of commercial paper;
(L) a certificate in or under a profit sharing or participation agreement;
(M) a certificate or instrument representing an interest in or under an oil, gas, or mining lease, fee, or title;
(N) a certificate or instrument representing or secured by an interest in any of the capital, property, assets, profits, or earnings of a company;
(O) an investment contract; and
(P) any other instrument commonly known as a security, regardless of whether the instrument is similar to another instrument listed in this subsection; and
(2) applies regardless of whether the security is evidenced by a written instrument.[23]

In most cases whether a security was involved carries no controversy. For example, stock and limited partnership interests are both specifically listed in the Texas Securities Act securities definition. But other categories of securities require judicial interpretation and are themselves subject to court-derived definitions. Business attorneys should know several of these items and certain Texas idiosyncrasies. Further, business attorneys should specially note that interests in limited liability companies are not included in the list, thus whether an LLC interest is a security requires a review of the judicially adopted "investment contract" elements. The following is a non-comprehensive summary of certain commonly used judicial interpretations of the definition of "security" in the Texas Securities Act.

Investment Contract

[23] Tex. Gov't Code §4001.068(a).

The Recodified TSA's definition of "security" includes investment contracts.[24] The definition of "investment contract" stems from two seminal Supreme Court cases from 1943 and 1946, *SEC v. C.M. Joiner Leasing Corp.*[25] and *SEC v. W.J. Howey Co.*[26] *C.M. Joiner Leasing Corp.* held that even if the sale of oil and gas leases was not a security, the sale of oil and gas leases coupled with the commitment that the Joiner Company was engaged to drill the test well was an investment contract. The Supreme Court determined that the C.M. Joiner Leasing Corp. transaction was a "investment contract" by asking "is what character the instrument is given in commerce by the terms of the offer, the plan of distribution, and the economic inducements held out to the prospect."[27] *W.J. Howey Co.* involved a promoter selling portions of a large citrus grove "coupled with a contract for cultivating, marketing and remitting the net proceeds to the investor."[28] The Supreme Court reversed a holding that the grove interests were not securities and established the still-used test as to whether a transaction is an investment contract. The Supreme Court stated:

> The test is whether the scheme involves an investment of money in a common enterprise with profits to come solely from the efforts of others. If that test be satisfied, it is immaterial whether the enterprise is speculative or nonspeculative, or whether there is a sale of property with or without intrinsic value.[29]

In 2015, the Texas Supreme Court issued a lengthy 14,000-word opinion holding that fractional interests in life settlement contracts were securities in the form of investment contracts under the Texas Securities Act in *Life Partners v. Arnold*.[30] The Court thoroughly reviewed the history of the *Howey*-derived investment contract test and interpretation of each element of the test. The Court held:

> (W)e conclude that three key principles must guide our construction and application of the term "investment contract." First, we must broadly construe the term to maximize the protection the Act is intended to provide to the investing public. Second, we must focus on the economic realities of the transaction at issue. And third, if the economic realities establish that a transaction is an investment contract, we must apply the statute regardless of any labels or terminology the parties may have used. In light of these principles, we conclude that **an "investment contract" for purposes of the Texas Securities Act means (1) a contract, transaction, or**

[24] Tex. Gov't Code §4001.068.
[25] *S.E.C. v. C. M. Joiner Leasing Corp.*, 320 U.S. 344, 64 S. Ct. 120, 88 L. Ed. 88 (1943).
[26] *S.E.C. v. W.J. Howey Co.*, 328 U.S. 293, 301, 66 S. Ct. 1100, 90 L. Ed. 1244 (1946).
[27] *S.E.C. v. C. M. Joiner Leasing Corp.* at 352–53.
[28] *S.E.C. v. W.J. Howey Co.* at 294.
[29] *S.E.C. v. W.J. Howey Co.* at 298–99.
[30] *Life Partners, Inc. v. Arnold*, 464 S.W.3d 660 (Tex. 2015).

> **scheme through which a person pays money (2) to participate in a common venture or enterprise (3) with the expectation of receiving profits, (4) under circumstances in which the failure or success of the enterprise, and thus the person's realization of the expected profits, is at least predominately due to the entrepreneurial or managerial, rather than merely ministerial or clerical, efforts of others, regardless of whether those efforts are made before or after the transaction.**[31] (emphasis added).

Common Venture or Enterprise

Cases under the Texas Securities Act require either horizontal or vertical commonality to satisfy the common enterprise element of the investment contract test. Horizontal commonality relates to the pooling of investor funds. "Horizontal commonality is between investors and means that the success of one investor is concomitant with the success of other investors."[32] Vertical commonality is "common enterprise between investor and promoter, so that the success of the investor is dependent upon the efforts and success of the promoter."[33]

Expectation of Receiving Profits from the Efforts of Others

The Texas Supreme Court focused on the investment contract definition's "from the efforts of others" prong in the *Life Partners v. Arnold* case. The Court focused on three principles: 1) Courts must broadly construe the term "investment contract" to maximize the protection the Texas Securities Act provides to the investing public; 2) Courts must focus on the economic realities of the transaction to determine whether it meets the investment contract test's requirements, and 3) if the economic realities satisfy the requirements of the investment contract test, the Court must conclude that the transaction is an investment contract regardless of the labels or terminology used to describe the transaction.[34] Then, the Texas Supreme Court addressed "profit from the efforts of others" – addressing two elements "profits" and "from the efforts of others" at once:

> (W)ith the expectation of receiving profits, under circumstances in which the failure or success of the enterprise, and thus the person's realization of the expected profits, is at least predominately due to the entrepreneurial or managerial, rather than merely ministerial or clerical, efforts of others. . . . And third, we hold that the

[31] *Id.* at 667.
[32] *Searsy v. Commercial Trading Corp.*, 560 S.W.2d 637, 639 (Tex. 1977); *see also King Commodity Co. v. State*, 508 S.W.2d 439, 442 (Tex. Civ. App. 1974).
[33] *Searsy v. Commercial Trading Corp.*, at 639; *Morgan v. State*, 644 S.W.2d 766, 771 (Tex. App.—Dallas 1982), rehearing denied; *Clayton Brokerage Co. v. Mouer*, 520 S.W.2d 802, 806–07 (Tex. Civ. App.—Austin 1975); *cf Cross v. DFW South Entry P'ship*, 629 S.W.2d 860, 863 (Tex. App.—Dallas 1982).
[34] *Life Partners, Inc. v. Arnold*, 464 S.W.3d 660, 670 (Tex. 2015).

> entrepreneurial or managerial efforts that are relevant to this inquiry, whether those of the purchasers or of others, include those that are made prior to the transaction as well as those that are made after.[35]

The "profit" element of the investment contract test is satisfied by both expected variable and fixed rate returns.[36]

The "efforts of others" element of the investment contract test revolves around "the entrepreneurial or managerial efforts of others"[37] or "the kinds of efforts that are 'significant' when applying the test are 'essential managerial efforts.'[38] Texas courts should "determine whether the purchaser enjoyed or exercised control over the asset or the operations of the enterprise, such that the purchaser would fulfill a 'managerial' or 'operational' role."[39] Note the Texas Supreme Court's use of the disjunctive in "enjoyed or exercised." "Exercised" captures business structures in which the investors have substantive authority to manage or operate the issuer's business, but in fact such management decisions and operations are conducted by someone else. The Texas Supreme Court adopted the Fifth Circuit's approach of *Long v. Schultz Cattle Co.* in *Life Partners* which can be summarized:

> the plaintiffs, who invested in a cattle-raising operation, "had a substantial degree of theoretical control over their investment. They could, theoretically, move their cattle to a different feedyard, decide what to feed them, provide their own veterinary care, or seek buyers on their own," and in fact they "were required to authorize every management decision involving their cattle.". . . But "the evidence [was] undisputed that at each juncture plaintiffs relied solely on the [seller's] advice" and followed all of the seller's recommendations. . . . Thus, "even if [the purchasers] technically made the key management decisions, they simply rubber-stamped [the seller's] recommendations and relied entirely on [the seller's] efforts and expertise to manage the underlying venture."[40]

"Enjoyed" could be interpreted to capture issuer business structures in which the someone (other than the investors) has substantive authority in the issuer's governing documents to manage or operate the business, but, in reality, failed to do so. But this interpretation could run into the Texas Supreme Court's "economic reality" approach to the investment contract test. Regardless,

---

[35] *Life Partners, Inc.* at 681.
[36] *S.E.C. v. Edwards*, 540 U.S. 389, 397, 124 S. Ct. 892, 157 L. Ed. 2d 813 (2004); *Life Partners v. Arnold* at 670.
[37] *Howey*, 421 U.S. at 852; *Life Partners, Inc.* at 673.
[38] *Searsy v. Commercial Trading Corp.*, 560 S.W.2d 637, 641 (Tex. 1977); *Life Partners, Inc.* at 673.
[39] *Life Partners, Inc.* at 674, citing *Banghart v. Hollywood Gen. P'ship*, 902 F.2d 805, 807 (10th Cir. 1990); *Siebel v. Scott*, 725 F.2d 995, 999 (5th Cir. 1984).
[40] *Long v. Shultz Cattle Co.*, 881 F.2d 129–36 (5th Cir. 1989).

the "efforts of others" element of the investment contract test will require a close analysis of the issuer's governing documents and the actual manner in which the issuer's business and operations were represented to investors as planned to be conducted or were actually conducted. Such factually intensive inquiries may result in such matters getting past motions for summary judgment on whether the investment contract test has been satisfied or the evidence has fallen short.

The Texas Supreme Court held in *Life Partners* that ministerial and clerical operations do not count for control. It held that:

> [T]o constitute an investment contract under the "efforts" aspect of the *Howey/Forman* test, the transaction must be such that, in reality, the seller, or another party other than the purchaser, exercises the predominate managerial or entrepreneurial control on which the purchaser's anticipation of profits is based. Conversely, courts have recognized that control over merely "ministerial" or "clerical" functions does not constitute the kind of "significant efforts" that satisfy the *Howey/Forman* test.[41] (citations omitted).

Finally, the Texas Supreme Court determined in *Life Partners* that the efforts of others that pre-date the offer or sale of the alleged securities count in determining the satisfaction of the investment contract test's "efforts of others" element.

Debt Securities

The Texas Securities Act's "securities" definition includes debt obligations, including: "a note, bond, debenture, mortgage certificate, or other evidence of indebtedness."[42] Bonds, debentures and mortgage certificates are fairly apparent and have not been involved in much litigation on the definition of "securities" under the Texas Securities Act. But, "notes" and "other evidence of indebtedness" have been the focus of litigation. We will start with "evidence of indebtedness."

[41] *Life Partners, Inc.* at 674.
[42] Tex. Gov't Code §4001.068.

Evidence of Indebtedness

In 1996, the Texas Court of Criminal Appeals reviewed the meaning of "evidence of indebtedness" under the Texas Securities Act's definition of "security" in *Thomas v. State*.[43] The Texas Court of Criminal Appeals adopted and expanded upon a definition used by the Texas Supreme Court in 1977's *Searsy v. Commercial Trading Company Corp*.[44] In *Searsy*, the Texas Supreme Court held that "evidence of indebtedness" meant "all contractual obligations to pay in the future for consideration presently received."[45] The Texas Court of Criminal Appeals narrowed that definition, holding that: "the term must be applied in light of the underlying purpose of the Act, to 'protect investors.'"[46] The Court of Criminal Appeals' writings from *Thomas* on this issue is included in the footnotes.[47]

---

[43] *Thomas v. State*, 919 S.W.2d 427. 431–32 (Tex. Crim. App. 1996) (Note that the author was the original investigator and wrote the Texas Securities Commissioner's amicus brief to the Court of Criminal Appeals in this case).

[44] *Searsy v. Commercial Trading Co. Corp*., 560 S.W.2d 637 (Tex. 1977).

[45] *Searsy* at 641.

[46] *Thomas* at 432.

[47] Having disapproved of the Court of Appeals' definition of "evidence of indebtedness," we are now faced with the further question of how the phrase should be defined. The State urges this Court to apply the definition ascribed by the Texas Supreme Court in *Searsy*, supra. In *Searsy*, the Supreme Court observed that "evidence of indebtedness" is a term taken from the Federal Act and has been defined by federal courts as "all contractual obligations to pay in the future for consideration presently received." *Searsy*, 560 S.W.2d at 641 (citing *United States v. Austin*, 462 F.2d 724, 736 (10th Cir.), *cert. denied*, 409 U.S. 1048, 93 S. Ct. 518, 34 L. Ed. 2d 501, 93 S. Ct. 545, 93 S. Ct. 547 (1972)). The Supreme Court held that although the options at issue there were subject to market fluctuations as to the amounts due or payable, they nevertheless represented "an obligation to pay . . . a monetary return at some future time." 560 S.W.2d at 642. Appellant contends the *Searsy* definition is too broad for use in the criminal context.

> Black's Law Dictionary defines "indebtedness" as:
>
> The state of being in debt, without regard to the ability or inability of the party to pay the same. The owing of a sum of money upon a certain and express agreement. Obligations yet to become due constitute indebtedness, as well as those already due. And in a broad sense and in common understanding the word may mean anything that is due and owing. *See also* Debt. BLACK'S LAW DICTIONARY 768 (6th ed. 1990). Notes, bonds, debentures, and mortgage certificates all evidence "the owing of a sum of money upon a certain and express agreement."

"The owing of a sum of money upon a certain and express agreement" is consistent with, but even broader than, *Searsy*'s definition of evidence of indebtedness, as *Searsy* requires consideration presently received. We hold that *Searsy*'s definition is consistent with a plain reading of the phrase "other evidence of indebtedness" as used in the context of section 4(A) and adopt the same as our own.

We accordingly interpret the phrase "evidence of indebtedness" to mean "all contractual obligations to pay in the future for consideration presently received." *Searsy*, supra. We emphasize that this definition is limited by the purposes of the Act itself and by the context in which it appears. That is, as discussed above, an evidence of indebtedness is a similar *type* of security as a note, bond, debenture, and mortgage certificate. In addition, the term must be applied in light of the underlying purpose of the Act, to "protect investors." We see no other way to reasonably interpret this provision, while remaining true to the plain language of the terms and consistent with the Act as a whole. Our holding is also consistent with the holdings of federal courts in interpreting this and other terms under the Federal Act. *See, e.g.*, *Llanos v. United States*, 206 F.2d 852, 854 (9th Cir. 1953)(recognizing promissory note as "clearly an evidence of indebtedness"), *cert. denied*, 346 U.S. 923, 98 L. Ed. 417, 74 S. Ct. 310 (1954); *United States v. Austin*, 462 F.2d 724, 736 (10th Cir.)(defining term "evidence of indebtedness" "to include all contractual

Notes as Securities

In 1990, the U.S. Supreme Court in *Reves v. Ernst & Young*[48] defined when a note was a security and when it was not a security in an incredibly complicated legal test that provides a daunting challenge to attorneys attempting to write jury charges. Indeed, the Supreme Court called this test the "family resemblance test," a name that does not encourage legal clarity. Texas Courts have followed *Reves*, although the Texas Supreme Court has never ruled on using *Reves* in connection with determining whether a note is a security.[49]

The Supreme Court in *Reves* said that the definition of a security should be treated broadly to capture a variety of investment schemes:

> Congress therefore did not attempt precisely to cabin the scope of the Securities Acts. Rather, it enacted a definition of "security" sufficiently broad to encompass virtually any instrument that might be sold as an investment . . . (W)e are not bound by legal formalisms, but instead take account of the economics of the transaction under investigation. Congress' purpose in enacting the securities laws was to regulate investments, in whatever form they are made and by whatever name they are called.[50]

The Supreme Court heavily based its *Reves* opinion and its adoption of the "family resemblance" test on a 1975 opinion by Judge Friendly of the Second Circuit.[51] The laundry list of exceptions to a note being a security created by Judge Friendly and adopted by the Supreme Court in *Reves* relate to, in Judge Friendly's word, "mercantile" transactions.

Under the "family resemblance" test, a note is presumed to be a "security," and that presumption may be preliminarily rebutted by a showing that it more closely resembles the "family" of instruments found not to be securities.[52] The *Reves* court listed the following categories of transactions where notes may not be securities:

1) the note delivered in consumer financing;

---

obligations to pay in the future for consideration presently received"), *cert. denied*, 409 U.S. 1048, 34 L. Ed. 2d 501, 93 S. Ct. 518, 93 S. Ct. 545, 93 S. Ct. 547 (1972); *United States v. Attaway*, 211 F. Supp. 682, 685 (W.D. La. 1962)(defining "securities" as "evidences of obligations to pay money, or of a right to participate in the earnings or distribution of property"); *S.E.C. v. Thunderbird Valley, Inc.*, 356 F. Supp. 184, 187 (S.D. S.D. 1973)(stating "the ordinary terms of 'any note' or 'evidence of indebtedness' are self-defining and require no further definition" and further that the term "security" should be viewed as flexible enough to "meet the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits"). *Thomas* at 431–32.

[48] *Reves v. Ernst & Young*, 494 U.S. 56, 110 S.Ct. 945, 108 L. Ed.2d 47 (1990).

[49] *Campbell v. Payne and Geldermann Sec., Inc.*, 894 S.W.2d 411, 417–18 (Tex. App.—Amarillo 1995); *Grotjohn Precise Connexiones Intern., S.A. v. JEM Fin., Inc.*, 12 S.W. 3d 859, 868 (Tex. App.—Texarkana 2000).

[50] *Reves v. Ernst & Young* at 61; *See also Campbell v. Payne and Geldermann Securities, Inc.* at 418.

[51] *Exchange National Bank of Chi. v. Touche Ross*, 544 F.2d 1126 (2nd Cir. 1975).

[52] *Trust Co. of La. v. N.N.P. Inc.*, 104 F.3d 1478, 1489 (5th Cir. 1997).

2) the note secured by a mortgage on a home;
3) the short-term note secured by a lien on a small business or some of its assets;
4) the note evidencing a 'character' loan to a bank customer;
5) short-term notes secured by an assignment of accounts receivable;
6) a note which simply formalizes an open-account debt incurred in the ordinary course of business (particularly if, as in the case of the customer of a broker, it is collateralized; and
7) notes evidencing loans by commercial banks for current operations.[53]

Then, if the instrument is not sufficiently similar to an item on the family resemblance list, four factors are examined to determine whether the instrument at issue is in another category that should be added to the list of non-securities.[54]

> First, we examine the transaction to assess the motivations that would prompt a reasonable seller and buyer to enter into it. If the seller's purpose is to raise money for the general use of a business enterprise or to finance substantial investments and the buyer is interested primarily in the profit the note is expected to generate, the instrument is likely to be a "security." If the note is exchanged to facilitate the purchase and sale of a minor asset or consumer good, to correct for the seller's cash-flow difficulties, or to advance some other commercial or consumer purpose, on the other hand, the note is less sensibly described as a "security." Second, we examine the "plan of distribution" of the instrument to determine whether it is an instrument in which there is "common trading for speculation or investment." Third, we examine the reasonable expectations of the investing public: The Court will consider instruments to be "securities" on the basis of such public expectations, even where an economic analysis of the circumstances of the particular transaction might suggest that the instruments are not "securities" as used in that transaction. Finally, we examine whether some factor such as the existence of another regulatory scheme significantly reduces the risk of the instrument, thereby rendering application of the Securities Acts unnecessary.[55]

As to the motivation of the parties, the Supreme Court held that a Court should "assess the motivations that would prompt a reasonable seller and buyer to enter into it." The Court said:

> If the seller's purpose is to raise money for the general use of a business enterprise or to finance substantial investments and the buyer is interested primarily in the profit the note is expected to generate, the instrument is likely to be a "security." If the note is exchanged to facilitate the purchase and sale of a minor asset or consumer good, to correct for the seller's cash-flow difficulties, or to advance some other commercial or consumer purpose, on the other hand, the note is less sensibly described as a "security."[56]

---

[53] *Reves v. Ernst & Young*, 494 U.S. at 61.
[54] *Trust Co. of La. v. N.N.P. Inc.* at 1489.
[55] *Reves v. Ernst & Young* at 61.
[56] *Id.* at 66.

Second, the Supreme Court in *Reves* held that a court should "examine the plan of distribution of the instrument to determine whether it is an instrument in which there is common trading for speculation or investment." The fact that there is not widespread public distribution does not mean a note is not a security. A debt instrument may be distributed to but one investor, yet still be a security.[57] For example, a Texas Court has held that the fact that an instrument was limited solely to two parties was, at best, inconclusive as to the instrument being a security:

> Upon its face, the instrument is limited to the parties to the transaction. However, there are no prohibitions on transfers of the instrument to persons who were not original parties to the transaction or prohibitions against trading in a secondary market.[58]

Third, the Supreme Court in *Reves* held a Court should examine "the reasonable expectations of the investing public." [59] That is, whether the public would reasonably view the note as an investment instrument, rather than a consumer or commercial bank loan?

Fourth and finally, the Supreme Court held in *Reves* that a court should look to the existence of another risk-reducing alternative regulatory scheme.[60] Examples of alternative risk-reducing regulatory schemes to provide any comfort to investors that their interests were being protected outside of a securities law regulatory regime are banking regulation, [61] CFTC commodity futures regulation, and state insurance administrators' insurance regulation.

Like the investment contract definition, the *Reves* family resemblance test is fact intensive and will involve multiple applications of facts to law. Thus, there may be little success with dispositive motions in cases where the determination of whether a note is a security is a significant issue.

Elements of Texas Securities Act Securities Fraud Claim against Sellers

Texas Securities Act securities fraud claims for primary liability against sellers and relevant defenses have the following elements:[62]

---

[57] *Trust Co. of La. v. N.N.P. Inc*., at 1489.
[58] *Grotjohn Precise Connexiones Intern., S.A. v. JEM Fin., Inc.*, 12 S.W.3d 859, 869 (Tex. App.—Texarkana 2000, no pet.).
[59] *Trust Co. of La. v. N.N.P. Inc*., at 1489.
[60] *Reves v. Ernst & Young* at 69.
[61] *See e.g. Marine Bank v. Weaver*, 455 U.S. 551, 559, 102 S. Ct., 1220 (1982) "It is unnecessary to subject issuers of bank certificates of deposit to liability under the antifraud provisions of the federal securities laws since the holders of bank certificates of deposit are abundantly protected under the federal banking laws."
[62] Tex. Gov't Code §4008.052.

a. A sale (or offer to sell) as defined by the Texas Securities Act;[63]
b. An instrument or transaction that is a security as defined by Texas Securities Act;[64]
c. The offer to sell or sale is made "by means of:" 1) an untrue statement; or 2) omission to state a fact;
d. The statement of fact or omitted fact is "material;"
e. Whether the omission is misleading depends on the "light of the circumstances under which they are made;"
f. The untrue statement or statement with a material omission needs to have been made to the plaintiff or the "by means of" requirement must be otherwise fulfilled; **AND**
g. The plaintiff must be in statutory privity with the defendant and must have purchased the security from the defendant who sold him or her the security.
h. Defendants have a defense if they sustain the burden of proof that:
   i. The seller knew of the untruth or omission, **OR**
   ii. The offeror or buyer did not know, and in the exercise of reasonable care could not have known, of the untruth or omission.[65]

This legal standard requires at least nine (9) separate applications of law to facts: seven (7) to prove the claim and two (2) to prove the defense.

Elements of Texas Securities Act Securities Fraud Claim against Purchaser

Texas Securities Act securities fraud claims for primary liability against purchasers and relevant defenses have the following elements:[66]

a. A purchase (or offer to buy) as defined by the Texas Securities Act;[67]
b. An instrument or transaction that is a security as defined by Texas Securities Act;[68]
c. The offer to buy or the purchase is made "by means of:" 1) an untrue statement; or 2) omission to state a fact;
d. The statement of fact or omitted fact is "material;"

[63] Tex. Gov't Code §4004.067.
[64] Tex. Gov't Code §4004.068.
[65] Tex. Gov't Code §4008.052.
[66] Tex. Gov't Code §4008.052.
[67] Tex. Gov't Code §4004.067.
[68] Tex. Gov't Code §4004.068.

e. Whether the omission is misleading depends on the "light of the circumstances under which they are made;"

f. The untrue statement or statement with a material omission needs to have been made to the plaintiff or the "by means of" requirement must be otherwise fulfilled; **AND**

g. The plaintiff must be in statutory privity with the defendant and must have purchased the security from the defendant who sold him or her the security.

h. Defendants have a defense if they sustain the burden of proof that:

i. The seller knew of the untruth or omission, **OR**

ii. The offeror or buyer did not know, and in the exercise of reasonable care could not have known, of the untruth or omission.[69]

This legal standard requires at least nine (9) separate applications of law to facts: seven (7) to prove the claim and two (2) to prove the defense.

Additionally, several of the elemental phrases applicable to both seller and buyer securities fraud claims, such as materiality and statutory privity, have court-adopted elements to define those terms. These caselaw elements are addressed below.

Materiality

Business attorneys should expect that one of the most litigated areas in a case under the Texas Securities Act will be the "materiality" of the alleged untrue statement or omission. Materiality determinations use objective reasonable person standards. "An omission or misrepresentation is material if there is a substantial likelihood that proper disclosure would have been viewed by a reasonable investor as significantly altering the total mix of information made available."[70] Alternatively, "[a]n omission or misrepresentation is material if there is a substantial likelihood that a *reasonable* investor would consider it important in deciding to invest." (emphasis in original).[71] These standards derive from the U.S. Supreme Court's federal securities law standards for materiality in a securities fraud case — "a substantial likelihood that the

[69] Tex. Gov't Code §4008.052.

[70] *Duperier v. Tex. State Bank*, 28 S.W.3d 740 (Tex. App.—Corpus Christi 2000, pet. dism'd); *Anheuser Busch Co., Inc. v. Summit Coffee Co*., 858 S.W.2d 928, 936 (Tex. App.—Dallas 1993, writ denied), *vacated by* 514 U.S. 1001, 115 S. Ct. 1309, 131 L. Ed. 2d 192 (1995) (remanded for reconsideration in light of *Gustafson v. Alloyd Co. Inc.*, 513 U.S. 561, 131 L. Ed. 2d 1, 115 S. Ct. 1061 (1995)), *on remand*, 934 S.W.2d 705 (Tex. App.—Dallas 1996, writ dism'd by agr.) (disposing of case in same manner as original appeal).

[71] *Weatherly v. Deloitte & Touche*, 905 S.W.2d 642, 649 (Tex. App.—Houston [14th Dist.] 1995, writ dism'd w.o.j.); see also *Highland Capital Mgmt., LP v. Ryder Scott Co.*, 402 S.W.3d 719, 743 (Tex. App.—Houston [1st Dist.] 2012, no pet.); *Tex. Cap. Sec., Inc. v. Sandefer*, 58 S.W.3d 760, 766 (Tex. App.—Houston [1st Dist.] 2001, pet. denied).

disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available."[72] The total mix of information element is important because "[a]ny approach that designates a single fact or occurrence as always determinative of an inherently fact-specific finding such as materiality, must necessarily be overinclusive or underinclusive."[73] Thus, the elements of the materiality standard for alleged and proven untrue or omitted facts can be formulated as follows:

1) Substantial likelihood;
2) Reasonable buyer or seller (depending on whether the claimant was the buyer or seller);
3) Omitted or untrue fact
4) Such fact significantly alters;
5) Total mix of information available.

Each of these elements requires separate consideration. From a probability perspective, was the "substantial likelihood" standard fulfilled? Did claimants act as "reasonable" buyers or sellers? Did whatever omitted or untrue facts claimants alleged and proved by a preponderance of the evidence provide significant alteration to the terms of the transaction? What was the total mix of information available? Finally, materiality is a mixed question of law and fact reserved for the trier of fact.[74]

Definition of "Sale"[75] as Applied in the Texas Securities Act's Private Causes of Action

"Link in the Chain of Sale" 1956 – 1977

The broad definition of "sale" in 4001.067 of the Recodified TSA states:

Sec. 4001.067. SALE; OFFER FOR SALE; SELL.

(a) "Sale," "offer for sale," and "sell" include every disposition or attempted disposition of a security for value.
(b) "Sale" means and includes:
  (1) a contract or agreement in which a security is sold, traded, or exchanged for money, property, or another thing of value; or
  (2) a transfer of or agreement to transfer a security, in trust or otherwise.
(c) "Sale" or "offer for sale" includes a subscription, an option for sale, a solicitation of sale, a solicitation of an offer to buy, an attempt to sell, or an offer to sell, directly or by an agent, by a circular, letter, or advertisement or otherwise, including the deposit in any

[72] *Matrixx Initiatives, Inc. v. Siracusano*, 563 U.S. 27, 38 (2011); *Basic Inc. v. Levinson*, 485 U.S. 224, 231–32 (1988).
[73] *Matrixx Initiatives, Inc. v. Siracusano* at 28 (quoting *Basic Inc. v. Levinson* at 236).
[74] *Highland Capital Mgmt., LP v. Ryder Scott Co.* at 744.
[75] Tex. Gov't Code §4004.067.

manner in the United States mail within this state of a circular, letter, or other advertising matter.

(d) **"Sell" means any act by which a sale is made**.

(e) A security given or delivered with or as a bonus on account of a purchase of securities or other thing of value is conclusively presumed to:
(1) constitute a part of the subject of the purchase; and
(2) have been sold for value.

(f) The sale of a security under conditions that entitle the purchaser or subsequent holder to exchange the security for another security or to purchase another security is not deemed a sale or offer for sale of the other security.

(g) This section does not limit the meaning of the terms "sale," "offer for sale," or "sell" as used by or accepted in courts.[76] (emphasis added).

"Any act by which a sale is made" is an incredibly broad standard. This standard was addressed by the Texas Supreme Court in 1956 in *Brown v. Cole*.[77] In this case, Brown accepted money for a securities subscription, forwarded 100% of the funds received to the issuer, and also invested for himself in the same offering. The Texas Supreme Court held:

> (T)he fact that Brown also became a purchaser and a participant does not ipso facto prevent his being a seller. Obviously, a dealer could purchase a part of the securities he offered for sale and sell a part to others. The provisions of the Securities Act are broad and comprehensive. Section 2(e) defines the term "sale," or "offer for sale" or "sell" as including "every disposition, or attempt to dispose of a security for value," and provides that "any security given or delivered with or as a bonus on account of, any purchase of securities or other thing of value, shall be conclusively presumed to constitute a part of the subject of such purchase and to have been sold for value." The Act further defines the term "sell" as meaning "any act by which a sale is made, and the term 'sale' or 'offer for sale' shall include a subscription, an option for sale, a solicitation of sale, an attempt to sell, or an offer to sell, directly or by an agent or salesman."
>
> Under the terms of the Act it is true that Kane was a seller, but if that fact alone would relieve petitioner of his responsibility then Kane could have denied acting in the capacity of a seller by showing that Fields was the seller. Clearly there may be more than one. **As we interpret the Act the seller may be any link in the chain of the selling process or in the words of the Act he is one who performs "any act by which a sale is made."** Suppose that Kane had agreed to pay Brown a commission on securing the participation of respondents and others in this venture, then it could hardly be denied that under the facts here shown Brown would have earned that commission because his efforts resulted in the participation by respondents.[78] (emphasis added).

[76] Tex. Gov't Code §4004.067.
[77] *Brown v. Cole*, 291 S.W.2d 624 (Tex. 1956).
[78] *Id.* at 629.

This "link in the chain of sale" interpretation from the Texas Supreme Court subsequently led to Texas Securities Act liability for numerous parties who, in reality, had little to do with the securities transaction. For example, in 1964, the Austin Court of Civil Appeals upheld a personal liability judgment against "Mrs. Millar" based on her role in the securities transaction as the person who provided the trade confirmation on behalf of the broker-dealer. Mrs. Millar had nothing to do with the sales process, but she signed the transmittal letter on the trade confirmation so she was held jointly and severally liable.[79] The late SMU securities law professor Alan Bromberg described a criminal case involving Gary Dean:

> In *Dean v. State* Gary Dean was deemed a seller to the Henrys of an override contract in the VibroSeat Company, although Ms. Lindsey (who was a cousin to the Henrys and often consulted with them on investments) initially suggested the investment to them, and although the Henrys decided to buy before even meeting Dean. Dean had no connection to the company except that he owned an override contract himself and supplied mechanical parts for the company. At the request of the company president, Dean closed the deal with the Henrys at a meeting arranged by Ms. Lindsey. At the meeting Dean "disclosed the particulars of" the Company to the Henrys, signed an override contract as representative of the company, received the Henrys' check (payable to the company) and handed it to Ms. Lindsey, who delivered the check to the company president. The Henrys testified that they had decided to buy before they met Dean, and that his representations at the meeting were not a procuring cause of their purchase.[80] Why he was ever prosecuted on the facts is something of a mystery.[81]

Another example of a concerning case was *Cherb v. Weber, Hall, Cobb & Caudle, Inc.*[82] in which the jury found that the defendant had used reasonable care and was innocently unaware of the untrue statements and omissions but was still held liable for violations of the Texas Securities Act.[83]

Statutory Privity for primary liability 1977 – 2021 in connection with a "sale" – End of "link in the chain of sale"

In 1976-1977, members of the Securities Committee of the State Bar of Texas Business Law Section were concerned about the link in the chain of sale case law, especially in cases

---

[79] *Christie v. Brewer*, 374 S.W.2d 908, 917 (Tex. Civ. App.—Austin 1964, writ ref'd n.r.e).
[80] Alan R. Bromberg, *Civil Liability under Texas Securities Act §33 (1977) and Related Claims*, 32 SW. L. J. 867, 882 (1978); *Dean v. State*, 433 S.W.2d 173 (Tex. Crim. App. 1968).
[81] *Bromberg.*, at 882 n.41.
[82] C*herb v. Weber, Hall, Cobb & Caudle, Inc.*; CCH Blue Sky Reporter ¶71,250 (N.D. Texas 1974).
[83] Hal M. Bateman, *Securities Litigation: The 1977 Modernization of Section 33 of the Texas Securities Act*, 15 HOUS. L. REV. 839, 843 (1978); Alan R. Bromberg, *Civil Liability under Texas Securities Act §33 (1977) and Related Claims*, 32 SW. L. J. 867 (1978).

targeting clearing firms and settlement agents whose involvement in the securities transactions was merely ministerial executions unrelated to the how the investment decision was made. In 1977 the Texas Legislature amended the private civil liability provisions of the Texas Securities Act to add additional legal burdens on making claims against those who are not in statutory privity with the claimants. The statutory "privity" standard includes brokers who actually made statements to the alleged aggrieved party,[84] as well as the specific counterparty in the securities transaction. Such statutory privity replaced the "link in the chain of sale" standard from *Brown v. Cole* and thus did not include clearing firms involved in the settlement of trades made through an introducing broker-dealer.[85] The privity standard comes from the text of the 1977 amendments to the Texas Securities Act. Then-Section 33.A of the Texas Securities Act required those held primarily liable to have been "to the person selling the securities **to him**" (emphasis added).

The Fourteenth Court of Appeals in Houston stated in 2000:

> The comments to the 1977 revisions to the Act contain the notation that the section in question (Section 33.A) "is a privity provision, allowing a buyer to recover from his offeror or seller . . ." The comment goes on to note that "some nonprivity defendants may be reached" under other sections of the Act not applicable here. Commentators at the time of revision had little doubt that the revision was intended to contain a privity provision. *See* Hal M. Bateman, *Securities Litigation: The 1977 Modernization of Section 33 of the Texas Securities Act*, 15 HOUS. L. REV. 839, 847 (1978).
>
> Nevertheless, appellants argue that *Brown v. Cole, 155 Tex. 624, 291 S.W.2d 704 (1956)* is applicable to this case and makes the underwriters liable to them. In *Cole*, the Texas Supreme Court defined the term "seller" broadly, making liable to an aggrieved buyer any person who served as a "link in the chain of the selling process." *Id. at 629, 291 S.W.2d at 708*. The appellants' reliance on *Cole* is undermined, however, by the fact that the statute has been significantly amended twice since that case was decided. Under the 1977 amendments the liability for "control persons and aiders" was incorporated into a new section of the statute; the comment pertinent to that section notes that "*Brown v. Cole* should have no application to the new law, since § 33F provides quite specifically who, besides a person who buys or sells, is liable, and the criteria for such liability." Guided by this comment, we look to see if § 33F of the Act supports liability for these defendants.

---

[84] *Texas Cap. Sec., Inc. v. Sandefer*, 58 S.W.3d 760, 776 (Tex. App.—Houston [1st Dist.] 2001, writ denied); *Lutheran Bhd. v. Kidder Peabody & Co.*, 829 S.W.2d 300, 306–07 (Tex. App.—Texarkana 1992, pet. granted, judgm't vacated w.r.m.).

[85] *Frank v. Bear Stearns*, 11 S.W.3d 380, 383 (Tex. App.—Houston [14th Dist.] 2000, pet. denied). Note that before the 1977 amendments to the Texas Securities Act, courts did find settlement agents liable under the Texas Securities Act's definition of sale based on the actions of other persons. – See *Christie v. Brewer*, 374 S.W.2d 908, 917 (Tex. Civ. App.—Austin 1964, writ ref'd n.r.e.).

> Defendants are liable under this section if they directly or indirectly control a seller, buyer or issuer of a security, 581--33F § 1, or if they directly or indirectly, with intent to deceive or defraud, materially aids a seller, buyer or issuer of a security. 581--33F § 2.[86]

Using comparable federal law, in 2012 the First Court of Appeals in Houston delineated the line between primary liability and secondary liability under then Texas Securities Act, thusly:

> [W]e conclude that a "seller" for Section 33(A)(2) purposes can include '[a] person who successfully solicits the purchase, motivated at least in part by a desire to serve his own financial interests or those of the securities owner.'[87]

This standard derives from the U.S. Supreme Court's *Pinter v. Dahl* decision from 1988. In *Pinter v. Dahl*, the Supreme Court held that a "seller" under Section 12(a)(1) of the Securities Act of 1933, outside of the securities vendor or its agent, was someone "who successfully solicits the purchase, motivated at least in part by a desire to serve his own financial interests or those of a security owner."[88] The "successfully solicits" is a statutory privity standard – just like Section 4008.052 of the Recodified TSA[89] and Sections 33.A.1 and 33.A.2

The statutory language for both Texas Securities Act then-Sections 33.A.1 and 33.A.2 limited primary liability only to those who to the "person who offers or sells a security," provided that the claimant is "the person buying a security from him." For sales transactions, claims against those who were not sellers in such privity must rely on the control person and aider provisions of then- of the Texas Securities Act.

Finally, *Brown v. Cole*'s "link in the chain of sale" standard for "sale" is still good law for actions by the Texas State Securities Board. The 1977 amendments imposed no limits on the agency, just on private litigants.

2022 Recodification

The 1977 Texas Securities Act amendments inserted privity requirements for primary liability by inserting "to him" and "from him" in the primary liability cause of action provisions.

---

[86] *Frank v. Bear Stearns*, 11 S.W.3d 380, 383 (Tex. App.—Houston [14th Dist.] 2000, pet. denied); *Highland Capital Mgmt., LP v. Ryder Scott Co.* at 740 n.13; *Newby v. Enron Corp.*, 540 F. Supp. 2d 759, 782 n.27 (S.D. Tex. 2007). *See also Newby v. Lay (In re Enron Corp Derivative & ERISA Litig.)*, 258 F. Supp. 2d 576, 608 (S.D. Tex. 2003).
[87] *Highland Cap. Mgmt., L.P. v. Ryder Scott Co.*, 402 S.W.3d 719, 742 (Tex. App.—Houston [1st Dist.] 2012) (quoting *Pinter v. Dahl*, 486 U.S. 622, 647 (1988)).
[88] *Pinter v. Dahl* at 647.
[89] Tex. Gov't Code §4008.052.

The 2019 recodification of the Texas Securities Act (effective January 1, 2022) is required to be non-substantive. The Recodified TSA replaced "to him" and "from him" with the gender-neutral: "a person who offers or sells a security and from whom another person buys the security is liable to the buyer of the security."[90] The statutory privity requirements for primary liability claims remain.

Elements of Aiding Claim

The Recodified TSA provides for a private cause of action for violations of the Act outside of the statutory "privity" requirement for primary liability, provided the plaintiff proves additional elements, including a culpable mental state for aiders. As to aiding, the Recodified TSA states:

> Sec. 4008.055(c). A person who directly or indirectly with intent to deceive or defraud or with reckless disregard for the truth or the law materially aids a seller, buyer, or issuer of a security is liable under Section 4008.051, 4008.052, 4008.053, or 4008.054 jointly and severally with the seller, buyer, or issuer and to the same extent as the seller, buyer, or issuer.[91]

"Materially aids" means "substantial assistance." The 1st Court of Appeals in Houston, 2nd Court of Appeals in Fort Worth, 3rd Court of Appeals in Austin, 4th Court of Appeals in San Antonio, 5th Court of Appeals in Dallas, and 14th Court of Appeals in Houston have all held that one element of the aider claim is: "the alleged aider rendered 'substantial assistance' in the violation" of the Texas Securities Act.[92]

Courts have treated substantial assistance in a fact-intensive matter and been critical of efforts to seek aider liability against those who did not participate in the securities transaction. For example, *Crescendo Investments v. Brice* involved the beneficial owners of the general partner of a limited partnership, which was a franchisor (the Brices). Two officers of the franchisor (other than the Brices) signed an international master franchise agreement for the franchise with "Hugh Scott." Scott then proceeded to raise funds from investors by selling securities, which were interests in the profits or gross revenues of Scott's international franchises.

---

[90] Tex. Gov't Code §4008.052.
[91] Tex. Gov't Code §4008.055(c).
[92] *Highland Capital Mgmt., LP v. Ryder Scott Co.* at 733; *Murphy v. Reynolds*, 2011 Tex. App. Lexis 7818 (Tex. App.—Fort Worth 2011); *Goldstein v. Mortenson*, 113 S.W.3d 769, 776 (Tex. App—Austin (2003); *Crescendo Inv. v. Brice*, 61 S.W.3d 465, 472 (Tex. App.—San Antonio 2001, no pet.); *Morgan Keegan & Co. v. Purdue Ave. Inv'rs LP*, 2016 Tex. App. Lexis 5268, 2016 WL 2941266 (Tex. App.—Dallas 2016); *Narnia Invs. Ltd. v. Harvestons Sec., Inc.* at *13; *Navarro v. Thornton*, 316 S.W.3d 715 (Tex. App.—Houston [14th District] 2011, no writ); *Frank v. Bear, Stearns & Co.*, 11 S.W.3d 380, 384 (Tex. App.—Houston [14th Dist.] 2000, pet. denied).

Scott eventually defaulted on his franchise obligations. Scott's investors sued the Brices and others. The Court found that the Brices did not substantially assist Scott in selling securities or diverting funds and upheld a directed verdict.[93]

Appellate courts have denied summary judgment motions based on substantial assistance in cases against a broker-dealer whose registered associated person sold an investment away from the firm in violation of firm policies and FINRA requirements[94] and an engineering company who prepared oil and gas reserve estimates for an SEC-reporting issuer.[95]

In 2005, the Texas Supreme Court addressed an aider's culpable mental state under the Texas Securities Act in *Sterling Trust Co. v. Adderley*.[96] This case involved an aiding claim against a trust company that custodied self-directed IRA accounts in which the IRA account owner had directed his IRA to invest in a Ponzi scheme. At trial the District Court did not allow for an instruction on any awareness requirement or culpable mental state, apparently confusing the standard for primarily liability with the standard for aiding liability. The investors argued on appeal that "reckless disregard may be shown even if the aider had no awareness of its role in an improper scheme."[97] The Texas Supreme Court rejected that approach and held that aider defendants can only be held liable if plaintiffs proved that these defendants had a "general awareness" of the fraudulent scheme. The Texas Supreme Court said:

> We disagree that the "reckless disregard" standard either imposes a lesser standard than the "general awareness" requirement or allows liability to be imposed for a mere failure to investigate. Instead, we conclude that the statute's use of the phrase "reckless disregard for the truth or the law" accords with the requirement that an aider must be aware of the primary violator's improper activities before it may be held liable for assisting in the securities violation. The Legislature's use of the phrase "reckless disregard" is consistent with a requirement of subjective awareness; at the time that the Legislature enacted the TSA, this Court had long held that "recklessness" required evidence of "conscious indifference" in the context of gross negligence. See *Rowan v. Allen*, 134 Tex. 215, 134 S.W.2d 1022, 1025 (Tex. 1940) (holding that "reckless disregard of the rights of [the] plaintiff" means "a conscious indifference to her rights or welfare").[98]

[93] *Crescendo Inv. v. Brice*, 61 S.W.3d 465, 473 (Tex. App.—San Antonio 2001, no pet.).
[94] *Narnia Invs. Ltd. v. Harvestons Secs., Inc*.
[95] *Highland Capital Mgmt., LP v. Ryder Scott Co* at 733.
[96] *Sterling Trust Co. v. Adderley*, 168 S.W.3d 835 (Tex. 2005).
[97] *Id.* at 840.
[98] *Id.* at 841.

The Texas Supreme Court continued:

> We conclude that the TSA's scienter requirement of "reckless disregard for the truth or the law" is similarly intended to impose a requirement of "recklessness in its subjective form," and this recklessness must be directly related to the primary violator's securities violation. When the Texas Legislature adopted the aider provision of the TSA, it explicitly stated that aider liability should be imposed "only if the aider has the requisite *scienter*."[99]

The Texas Supreme court concluded:

> We therefore hold that the TSA's "reckless disregard for the truth or the law" standard means that an alleged aider can only be held liable if it rendered assistance "in the face of a perceived risk" that its assistance would facilitate untruthful or illegal activity by the primary violator. In order to perceive such a risk, the alleged aider must possess a "general awareness that his role was part of an overall activity that is improper."[100] (citations omitted)

Thus, claimants against aiders under the Recodified TSA thus must prove the following elements by a preponderance of the evidence:

1) a primary violation of the Securities Act under Section 4008.051 (unlicensed brokers and investment advisers and unregistered securities), 4008.052 (seller liability for securities fraud), 4008.053 (buyer liability for securities fraud), or 4008.054 (a registered offering with a prospectus containing an untrue statement of a material fact or an omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they are made, not misleading);
2) the defendant had general awareness of its role in this violation;
3) the defendant rendered substantial assistance in this violation; and
4) the defendant either (a) intended to deceive the plaintiff securities purchasers or sellers or (b) acted with reckless disregard for the truth of the representations made by the primary violator.[101]

Elements of Control Person Claim

The Recodified TSA provides for a second private cause of action for violations of the Act outside of the "privity" requirement for primary liability for control persons. The control person liability provisions in the Recodified TSA states as follows:

[99] *Id.* at 842 (quoting Tex. Rev. Civ. Stat. Ann. art. 851-33, Comment – 1977 Amendment (Vernon Supp. 2004-2005).
[100] *Id.* at 842.
[101] *Narnia Invs., Ltd. v. Harvestons Sec., Inc.* at *14, *Navarro v. Thornton* at 720; *Frank v. Bear Stearns & Co*. at 384.

Sec. 4008.055. CONTROLLING PERSON . . . LIABILITY.

(a) Except as provided by Subsection (b), a person who directly or indirectly controls a seller, buyer, or issuer of a security is liable under Section 4008.051, 4008.052, 4008.053, or 4008.054 jointly and severally with the seller, buyer, or issuer and to the same extent as the seller, buyer, or issuer.

(b) The controlling person is not liable under Subsection a) if the controlling person sustains the burden of proof that the controlling person did not know, and in the exercise of reasonable care could not have known, of the existence of the facts by reason of which the liability is alleged to exist.[102]

The first element requires plaintiffs to prove a primary violation under Section 4008.051 (unlicensed brokers and investment advisers and unregistered securities), 4008.052 (seller liability for securities fraud), 4008.053 (buyer liability for securities fraud), or 4008.054 (a registered offering with a prospectus containing an untrue statement of a material fact or an omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they are made, not misleading).[103]

The second element relates to acting as a control person under Recodified TSA. The Fourteenth Court of Appeals in Houston and Dallas Court of Appeals adopted the Eighth Circuit's control person test: "that the defendant exercised control over the operations of the corporation in general, and that the defendant had the power to control the specific transaction or activity upon which the primary violation is predicated."[104] The Texarkana Court of Appeals added an additional element to this test relating to inducing and participating in the primary violation: "to make a prima facie case that the defendant is a control person, a plaintiff must prove that each had actual power or influence over the controlled person and that each induced or participated in the alleged violation," borrowing the standard from the Fifth Circuit.[105]

[102] Tex. Gov't Code §4008.055(a) and (b).
[103] *Id.* at 743.
[104] *Frank v. Bear Stearns*, 11 S.W.3d 380, 383–84 (Tex. App.—Houston [14th Dist.] 2000, pet. denied); *Barnes v. SWS Fin. Servs*, 97 S.W.3d 759, 763 (Tex. App.—Dallas, 2003, no pet), *Darocy v. Abildtrup*, 345 S.W.3d 129, 137 (Tex. App.—Dallas 2011, no pet.); *Metge v. Baehler*, 762 F.2d 621, 631 (8th Cir. 1985).
[105] *Tex. Cap. Sec., Inc. v. Sandefer*, 80 S.W.3d 260, 267–68 (Tex. App.—Texarkana 2002, pet. stricken); *Dennis v. Gen. Imaging, Inc*., 918 F.2d 496, 509 (5th Cir. 1990); *G. A. Thompson & Co. v. Partridge*, 636 F.2d 945, 958 (5th Cir. 1981).

Courts have held that major shareholders,[106] senior officers,[107] directors,[108] and investment advisers to investment funds[109] are control persons under the Texas Securities Act, but that lenders,[110] underwriters,[111] and FINRA broker-dealers carrying the registration of brokers selling away unapproved securities[112] are not. Courts have also looked to the actual control authority that the defendant has, and not implied authority. For example, Morgan Stanley's "Regional Director for the Southwest Region" was not found to be a control person of a Morgan Stanley broker because he did not directly supervise the broker and did not possess any control over the type of transactions upon which the primary violations were based.[113]

Third, control person liability has an affirmative defense that combines due diligence and a lack of knowledge.

Non-selling Issuer Liability – Registered Offerings

An issuer who has registered an offering with the U.S. Securities and Exchange Commission under the Securities Act of 1933 or with the Texas State Securities Board relating to transactions involving securities held by the issuer's stockholders for offer or sale by the owner of such securities can be found liable for "untrue statements or an omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they are made, not misleading" relating to the prospectus (registration statement) in connection with the securities transactions subject to the registration statement or prospectus.[114] This provision, in function, is a modified version of the statutory privity required by Texas Securities Act Sections 4008.051, 4008.052, and 4008.053, in that the issuer made the statements found to be materially untrue or to have omitted material facts, but made those statements in connection with registered securities sales by its stock or debt holders, not just for itself.

---

[106] *Busse v. Pacific Cattle Feeding Fund #1*, 896 S.W.2d 807, 815 (Tex. App.—Texarkana 1995) (majority shareholder and director).
[107] *Texas Cap. Sec., Inc.*, 80 S.W. 3d at 766.
[108] *Darocy v. Abildtrup*, at 135–37 (board member, secretary, treasurer and salesperson).
[109] *Morgan Keegan & Co. v. Purdue Ave. Inv'rs LP* at *22–25.
[110] *Segner v. Sinclair Oil & Gas Co.*, 2012 U.S. Dist. LEXIS 193617 *46–47 (N.D. Tex. 2012); *Sieb Family GP, LLC v. Bank of the Ozarks*, 2014 Tex. App. LEXIS 3010, *7–8 (Tex. App.—Dallas 2014, no pet.).
[111] *Frank v. Bear Stearns* at 383–84.
[112] *Barnes v. SWS Fin. Servs*, at 763; *cf. Fernea v. Merrill Lynch*, 2011 Tex. App. LEXIS 5286 (Tex. App.—Austin 2011).
[113] *Gonzalez v. Morgan Stanley*, 2004 U.S. Dist. LEXIS 26709 (W.D. Tex. 2004).
[114] Tex. Gov't Code §4008.054.

Securities Registration Claims

The Recodified TSA includes private causes of action against those who sell securities in unregistered offerings (provided that statutory privity has been satisfied and there is no applicable exemption).[115] Any party claiming an exemption from the securities offering registration requirements has the burden of proof to prove such exemption.[116] The most commonly-used securities registration exemptions relate to secondary market transactions[117] and SEC Regulation D, particularly SEC Rule 506,[118] which provides an exemption safe harbor under the Securities Act of 1933 and also pre-empts state securities registration requirements (other than filing an offering notice form and paying fees).[119] To prove the lack of securities offering registration, contact the Texas State Securities Board to obtain a sealed and signed certificate of the absence of a public record which would be self-authenticating in court.[120]

Claims Against Unregistered Brokers and Dealers

The Recodified TSA includes private causes of action against unregistered brokers and dealers who represent the seller of the securities, but not against those who represent the buyer.[121] Further, unregistered brokers may not bring actions relating to unpaid commissions unless such broker proves compliance with an exemption from the broker-dealer registration requirements.[122] (Two commonly-used broker-dealer registration exemptions relate to oil and gas interests and industry-related purchasers[123] and certain mergers and acquisitions broker-dealers[124]). Any party claiming an exemption from the broker-dealer registration requirements has the burden of proof to prove such exemption.[125] To prove the lack of registration, contact the Texas State Securities Board to obtain a sealed and signed certificate of the absence of a public record which would be self-authenticating in court.[126]

---

[115] Tex. Gov't Code §4008.051(a).
[116] Tex. Gov't Code §4001.153.
[117] Tex. Gov't Code §4005.019.
[118] 17 CFR §230.506.
[119] 15 U.S.C. §77r(b)(4) and §77r(c).
[120] Texas Rule of Evidence 902.
[121] Tex. Gov't Code §4008.051(a).
[122] Tex. Gov't Code §§4008.001, 4008.003.
[123] 7 TEX. ADMIN. CODE §109.14(d).
[124] 7 TEX. ADMIN. CODE §139.27.
[125] Tex. Gov't Code §4001.153.
[126] Texas Rule of Evidence 902.

Claims Against Investment Advisers – Registration and Anti-Fraud

Investment advisers and investment adviser representatives can be found liable for acting as unregistered investment advisers or investment adviser representatives or for violating the anti-fraud provisions of the Recodified TSA. First, business attorneys should understand who is deemed to be an investment adviser and who is not deemed to be an investment adviser or investment adviser representative under Sections 4001.059 and 4001.060 the Recodified TSA. Investment Advisers are:

1) Option One
    a. Those who engage in the business of advising another, directly or through publications or writing; and
    b. with respect to the value of securities or the advisability of investing, purchasing or selling securities for compensation[127]
2) Option Two
    a. Those who with compensation;
    b. as part of a regular business;
    c. issue or adopt analyses or a report concerning securities; and
    d. as may be further defined by TSSB rule. [128]

The Recodified TSA includes several statutory carveouts from this definition:

1) a bank or a bank holding company, as defined by the Bank Holding Company Act of 1956 (12 U.S.C. Section 1841 et seq.), that is not an investment company;
2) a lawyer, accountant, engineer, teacher, or geologist whose performance of the services is solely incidental to the practice of the person's profession;
3) a dealer or agent who receives no special compensation for those services and whose performance of those services is solely incidental to transacting business as a dealer or agent;
4) the publisher of a bona fide newspaper, news magazine, or business or financial publication of general and regular circulation; or
5) a person whose advice, analyses, or report does not concern a security other than a security that is:
    a. a direct obligation of or an obligation the principal or interest of which is guaranteed by the United States government; or
    b. issued or guaranteed by a corporation in which the United States has a direct or indirect interest and designated by the United States Secretary of the Treasury under Section 3(a)(12), Securities Exchange Act of 1934 (15 U.S.C. Section 78c(a)(12)), as an exempt security for purposes of that Act.

[127] Tex. Gov't Code §4008.059.
[128] Tex. Gov't Code §4008.059.

The statutory carveout for the publisher of a bona fide newspaper, news magazine, or business or financial publication of general and regular circulation language was borrowed from the Supreme Court's 1985 decision in *Lowe v. SEC*, which applied First Amendment protections to statements by publishers relating to the purchase and sale of securities which are bona fide (genuine), of general and regular circulation and do not offer individualized advice attuned to any specific portfolio or to any client's particular needs.[129]

An "investment adviser representative:"

> includes a person or company who, for compensation, is employed, appointed, or authorized by an investment adviser to solicit clients for the investment adviser or who provides investment advice, directly or through subagents, as defined by Board rule, to an investment adviser's clients on behalf of the investment adviser.[130]
>
> Investment adviser representative does not include a partner of a partnership or officer of a corporation or other entity that is registered as an investment adviser under this title solely because of the person's status as a partner or officer of that entity.[131]

Clients have private causes of action under the Recodified TSA against unregistered investment advisers and investment adviser representatives (unless exempt).[132] Damages for such claims are limited to the advisory fees paid by the Clients.[133] Clients also have private causes of action against investment advisers and investment adviser representatives "who commit fraud or engages in a fraudulent practice in rendering services as an investment adviser."[134] The Recodified TSA defines "fraud" and "fraudulent practice" as:

> **Sec. 4001.058. Fraud; Fraudulent Practice.**
> (a) "Fraud" and "fraudulent practice" include:
> (1) a misrepresentation of a relevant fact made in any manner;
> (2) a promise, representation, or predication as to the future not made honestly and in good faith;
> (3) an intentional failure to disclose a material fact;
> (4) a direct or indirect gain, through the sale of a security, of an underwriting or promotion fee or profit, or of a selling or managing commission or profit, that is so gross or exorbitant as to be unconscionable; and

[129] *Lowe v. SEC*, 472 U.S. 181 (1975).
[130] Tex. Gov't Code §4008.060(a).
[131] Tex. Gov't Code §4008.060(b).
[132] Tex. Gov't Code §4008.101(a).
[133] Tex. Gov't Code §4008.101(a).
[134] Tex. Gov't Code §4008.101(b).

(5) a scheme, device, or other artifice to obtain a profit, fee, or commission described by Subdivision (4).

(b) Nothing in this section limits the full meaning of "fraud," "fraudulent," or "fraudulent practice" as applied or accepted in courts.[135]

Plaintiffs who have successfully proven fraud or fraudulent practice by an investment adviser or investment adviser representative may recover damages in the amount of: (1) of any consideration paid for the services, less the amount of any income the purchaser received from acting on the services, (2) any loss incurred by the purchaser in acting on the services provided by the investment adviser or investment adviser representative, (3) statutory interest and (4) court costs and reasonable attorney fees to the extent that the Court considers equitable.[136]

Claims alleging the defendant acting as an unregistered investment adviser or unregistered investment adviser representative have a three year statute of limitations with no discovery rule.[137] Claims alleging the defendant committed investment adviser or investment adviser representative fraud have a statute of limitations that is the longer of either five years or three years after the date the plaintiff knew or should have known, by the exercise of reasonable diligence, of the occurrence of the violation of the Recodified TSA investment adviser and investment adviser representative fraud and fraudulent practice.[138]

Remedies

The seller liability provisions for seller's securities fraud, buyer's securities fraud, securities registration and securities broker-dealer registration, aider, control person, and non-selling issuer claims is rescission or damages (if the buyer no longer owns the security).[139] Courts have followed the Texas Securities Act's use of the alternative "or" (rather than the accretive "and") and determined that the rescission and damages remedies are mutually exclusive. The remedy must be one or the other.[140] Control person and aider liability is joint and several with the seller or the buyer, depending on who such claims may be made against.[141] In addition to

[135] Tex. Gov't Code §4001.058.
[136] Tex. Gov't Code §4008.103.
[137] Tex. Gov't Code §4008.104(a).
[138] Tex. Gov't Code §4008.104(b).
[139] Tex. Gov't Code §§4008.051. 4008.052, 4008.053, 4008.054, and 4008.055.
[140] *Higbee v. Bridgestone Healthcare Mgmt.*, 2002 Bankr. Lexis 2009, at *19 (N.D. Tex. 2002); *Aegis Ins. Holding Co., LP v. Gaiser*, 2007 Tex. App. LEXIS 2364, at *8–12; 2007 WL 906328 (Tex. App.—San Antonio 2007, pet. denied).
[141] Tex. Gov't Code §4008.055.

rescission or damages, claimants shall also recover costs.[142] Further, the claimants may also recover attorneys' fees if the court finds that such recovery is equitable under the circumstances.[143]

> In determining whether an award of attorney's fees is equitable and what amount is equitable, "[a]ll the circumstances should be considered," including: (1) the conduct of the defendant in the transaction, including whether the conduct was fraudulent; (2) the conduct of the plaintiff in the transaction; (3) the conduct of both parties in the lawsuit; (4) whether the defendant benefited from the securities violation; and (5) whether there was a special fiduciary relationship between the plaintiff and the defendant.[144]

Texas Securities Act Section 4008.056 defines "rescission" as the recovery of the consideration provided plus statutory interest. For rescission claims against non-selling issuers, the rescission price is the price the buyer paid or the price at which the security was offered to the public.

> Sec. 4008.056. RESCISSION.
> (a) On rescission under this subchapter, a buyer of a security shall, on tender of the security or a security of the same class and series, recover the consideration the buyer paid for the security plus interest on the consideration at the legal rate from the date the buyer made the payment, less the amount of any income the buyer received on the security.
> (b) On rescission under this subchapter, a seller of a security shall recover the security or a security of the same class and series, on tender of the consideration the seller received for the security plus interest on the consideration at the legal rate from the date the seller received the payment, less the amount of any income the buyer received on the security.
> (c) For a buyer suing under Section 4008.054, the consideration the buyer paid for the security is deemed to be the lesser of:
> (1) the price the buyer paid; or
> (2) the price at which the security was offered to the public.
> (d) A tender specified in this section may be made at any time before a judgment is entered.[145]

Texas Securities Act Section 4008.057 defines "damages" as the consideration paid for the security plus statutory interest and income received by the buyer. Sellers receive damages in the amount of the value of the security sold or the actual consideration received plus any income

---

[142] Tex. Gov't Code §4008.060(a);
[143] Tex. Gov't Code §4008.060(b); *Kubbernus v. ECAL Partners, Ltd.* 574 S.W.3d 444, 463 (Tex. App.—Houston [1st District] 2018).
[144] *Kubbernus v. ECAL Partners, Ltd.* at 486; *Morgan Keegan & Co. v. Purdue Ave. Inv'rs LP* at 463.
[145] Tex. Gov't Code §4008.056.

the buyer received from the security. For damages claims against non-selling issuers, the rescission price is the price the buyer paid or the price at which the security was offered to the public.

> Sec. 4008.057. DAMAGES.
> (a) In damages under this subchapter, a buyer of a security shall recover the consideration the buyer paid for the security plus interest on the consideration at the legal rate from the date the buyer made the payment, less the greater of:
> (1) the value of the security at the time the buyer disposed of the security plus the amount of any income the buyer received on the security; or
> (2) the actual consideration received for the security at the time the buyer disposed of the security plus the amount of any income the buyer received on the security.
> (b) In damages under this subchapter, a seller of a security shall recover the value of the security at the time of sale plus the amount of any income the buyer received on the security, less the consideration paid to the seller for the security plus interest on the consideration at the legal rate from the date of payment to the seller.
> (c) For a buyer suing under Section 4008.054, the consideration the buyer paid for the security is deemed to be the lesser of:
> (1) the price the buyer paid; or
> (2) the price at which the security was offered to the public.[146]

Conclusion.

The above survey is not comprehensive. Indeed, this paper is shorter than the Texas Supreme Court opinion in *Life Partners, Inc. v. Arnold.* It has focused on the elements of the Recodified TSA's claims and defenses but has not covered the application of those elements to any set of facts in any depth. Business attorneys need to be able to advise clients of the consequences of non-compliance with securities laws. Indeed, the Texas Securities Act's private cause of action are used routinely in securities-related demand letters and lawsuits.

[146] Tex. Gov't Code §4008.057.